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ECONOMIC INTELLIGENCE WEEKLY

7 May 1975

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Overview

The EC Is Seeking Guidelines for a Raw Materials Policy before the OECD ministerial meeting scheduled for 28 May. The Community is particularly sensitive to this issue because its members collectively import 60% to 100% of their supplies of most major raw materials.

Development of a unified EC approach is being retarded by difficulties of member states in working out individual positions. [redacted]

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Riyadh Is More Actively Managing Saudi Wealth. The new leaders are channeling increasing amounts into long-term assets and into those denominated in continental European, Canadian, and Japanese currencies at the expense of sterling. [redacted]

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Note: Comments and queries regarding the *Economic Intelligence Weekly* are welcomed. They may be directed to [redacted] the Office of Economic Research, Code 143, Extension 7892.

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SAUDI ARABIA: CHANGING INVESTMENT POLICY

New Saudi investment -- now running more than $1 billion a month -- is being channeled increasingly into longer term assets and into continental European, Canadian, and Japanese currencies rather than sterling assets. Placement in dollars has remained strong. The changes are primarily the result of the accession of new leaders in Riyadh, who are paying closer attention to the investment of surplus oil revenues. [redacted]

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New Leadership, New Directions

Under the passive policy of the late King Faysal and Anwar 'Ali, head of the Saudi Arabian Monetary Agency (SAMA) for 15 years, the Saudis deposited oil receipts in old and trusted banks in London and New York; these banks decided on the ultimate disposition of the funds. The deaths of Faysal and 'Ali have brought to the fore a less conservative financial leadership. Under Crown Prince Fahd, this group is taking a more active part in investment decisions, with the result that new funds are being placed more widely and for longer terms.

The Saudis are currently giving final approval to more than $300 million in direct loans -- primarily government-backed loans to publicly owned utilities and industries in Austria, Finland, and Norway. Similar loans to Canada and Sweden are being considered. Last year the Saudis placed direct loans only in Canada,

France, and the United Kingdom. Riyadh has also expressed an interest in buying long-term (chiefly three-year) government securities, with West German and US issues apparently preferred.

Investment in the private sector -- particularly in the United States -- is also receiving increased Saudi attention.

- At least two new investment accounts have been established since January for the purchase of US equities.
- SAMA has begun purchasing US corporate bonds and notes.
- SAMA is investing in yen-denominated bonds of Japanese public utilities.

Less Interest in Sterling Assets

Saudi interest in sterling has been declining since late 1974. In the fourth quarter, investment in sterling-denominated assets fell to less than 5% of total placements, compared with the 10% share of sterling in accumulated Saudi holdings. Purchases of sterling stopped two months ago. Most of the funds ordinarily going into sterling are being placed in German marks, Swiss francs, Canadian dollars, and Japanese yen. In April, more than 10% of all new investment was placed in assets denominated in those currencies.

Excessive concentration in European currencies will be avoided. Huge investments in one country would probably provoke capital controls, because governments would be unwilling to accept further appreciation of exchange rates. SAMA has already assured Bern that only small amounts of new investment will be placed in Swiss francs.

Changes in the Saudi investment pattern will have little impact on the value of the US dollar. Eighty-five percent of new funds is still being placed in dollar denominated assets, roughly the same proportion as during the fourth quarter.

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The role of private banks in petrodollar recycling will be trimmed if the Saudis continue to make investments of longer maturity and extend more loans directly to oil importing countries. Though still huge, the sums channeled through private banks would be reduced. The banks thus would be less exposed than otherwise to the risk of using short-term deposits as a basis for long-term loans. At the same time, the Saudis would acquire a larger stake in the economic health of oil importing nations. The main concern is how much weight Riyadh will give to political, as opposed to economic, factors in placing surplus funds. (Secret No Foreign Dissem)

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CUBA: SUGAR FINANCES ECONOMIC ADVANCES

Record world sugar prices and economic policy changes have put the Cuban economy on its soundest footing since Castro came to power in 1959. Havana is exploiting its improved situation to expand trade and political relations with the non-Communist world. Nonetheless, Cuba will remain fundamentally tied to the USSR for the remainder of the decade. A persistent drought, together with the recent fall in world sugar prices, will make economic growth less rapid in 1975 than in 1974.

Performance in 1974

Although Cuban officials exaggerated the improvement, most sectors of the economy did in fact register appreciable gains in 1974.

- Sugar output increased about 8% over 1973, with the return of more normal weather during the growing season.

- Record sugar prices and a 13% rise in the volume of sugar exports led to a doubling of total exports to $3 billion, yielding a trade surplus of $350 million, the first since the Castro takeover.

- Construction activity rose about 10%, reflecting the building of transportation facilities, industrial plants, and housing.

Improved management played a considerable part in this performance. Since the disruptive 1969/70 drive to increase sugar output at all costs, Havana has rationalized economic controls through (a) more orthodox planning and cost accounting procedures, (b) greater use of material incentives to encourage worker productivity, and (c) strictly enforced antivagrancy laws to reduce worker absenteeism. In addition, progressive mechanization of the sugar harvest has reduced the problems stemming from widespread recruitment of "volunteer" cane cutters.

Expanding Western Trade and Credits

Bolstered by increasing hard currency earnings and trade credits, Cuban imports from the non-Communist world more than doubled in 1974, to nearly 40% of total imports. Increased imports of complete industrial plants and transportation equipment are providing a much needed fillip to the modernization of the domestic economy. Since late 1974, Cuba has secured about $350 million in French trade credits, $900 million in Spanish credits, and $100 million from Canada. Cuba's growing non-Communist trade has further eroded US and OAS sanctions and has tightened pressure on US foreign subsidiaries to do business with Havana.

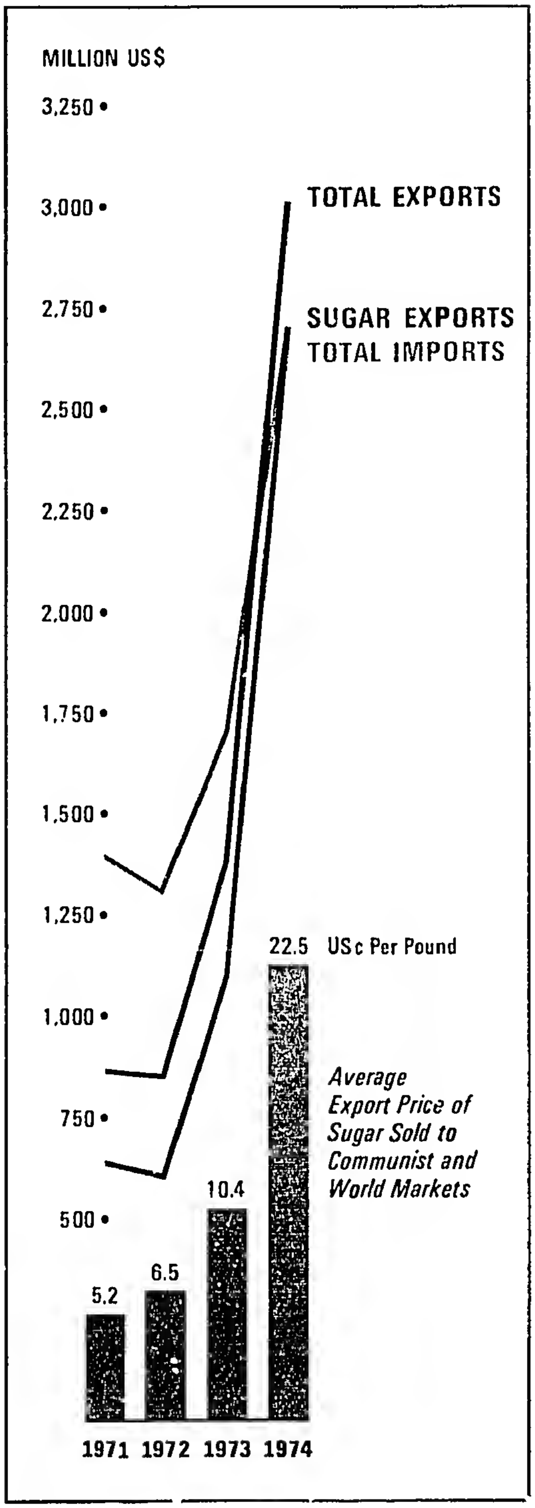
The Castro government has expressed a growing interest in re-establishing trade with the United States to gain increased access to US products and technology. Anti-US propaganda has been toned down considerably, and Cuban efforts to promote revolution in Latin America remain at a low ebb. Also, Havana may now be more flexible in its one standing precondition for talks with the United States, namely, unilateral termination of the US economic embargo.

Cuban-Soviet Ties

Economic gains have not eliminated the need for Soviet aid. Moscow still accounts for two-fifths of Cuban trade and satisfies practically all petroleum requirements at about one-half the world price. Soviet aid to Cuba proceeds under a $370 million commitment made in 1972 to Castro. The agreement also postponed

CUBAN FOREIGN TRADE:

VALUE AND PRICE



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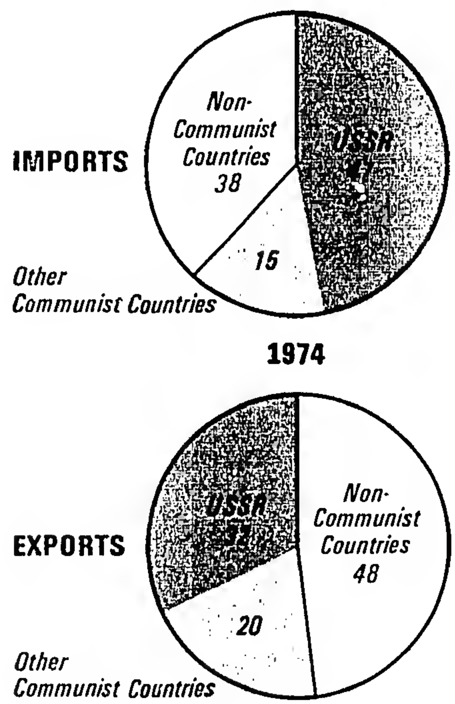
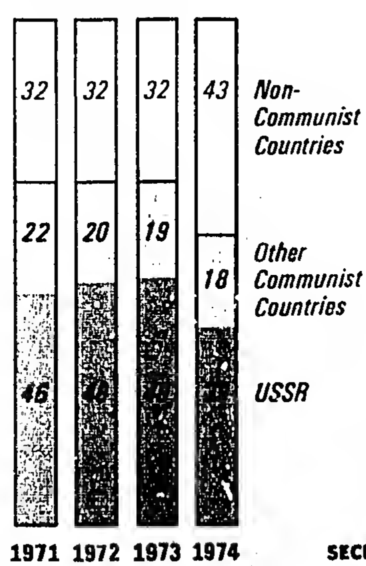
DIRECTION

PERCENT



TOTAL CUBAN TRADE



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the repayment of Cuba's debt to the USSR -- now estimated at $4.4 billion -- until 1986. In any case, the trade surplus promises to be short-lived, reenforcing Havana's dependence on Soviet assistance.

Prospects for 1975

Persistent drought during the 1974/75 growing season is expected to cut 1975 sugar output at least 5% below last year. Prospects for other crops are also dimmed by drought. At the same time, most of the nonagricultural sectors should remain strong. The Cuban people will have to remain patient, since time is needed for investment and modernization to be translated into additional consumer goods.

Cuba's trade surplus is expected to disappear in 1975 because of a rise in imports, buttressed by recent Western credits. Despite a 50% increase in the Soviet price for Cuban sugar, lower world prices and the reduction of Cuban sugar exports to about 5 million tons will hold export earnings close to last year's $3 billion.

While reduced agricultural output in 1975 will dampen growth temporarily, the continued investment program, the expansion of import capacity, and the improvements in management will ensure economic momentum over the next several years. With an assist from Western and Soviet lenders, Havana will emphasize industrial and agricultural investment in the Five-Year Plan, to begin in 1976. Equally important, the increasingly purposeful Castro government is unlikely to shift its game plan as it has been prone to do in the past. (Secret No Foreign Dissem)■

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SINGAPORE: BRIGHT SPOT IN SOUTHEAST ASIA

Singapore's Prime Minister Lee Kuan Yew, due in town this week for an unofficial meeting with President Ford, will urge continued US private investment in Southeast Asia. The strong performance of the Singapore economy in 1974 and Lee's natural sense of independence should minimize appeals for other support. At the same time, Lee will be able to engage in candid and wide-ranging exchanges on such issues as Indochina and US oil policy.

Economic Successes

Unlike many Asian countries, Singapore has withstood the energy crisis and world recession with remarkable success. Real economic growth in 1974 came to

an impressive 6.8%. Although well below the 11%-15% annual rates of 1966-73, it dispelled fears of a serious downturn in an economy heavily dependent on oil refining, entrepot trade, and financial intermediation. Soaring prices – especially for petroleum products – drove exports up 59% to $5.9 billion in the face of a 3% decline in volume. Imports rose 63% in value to $8.5 billion, almost entirely the result of stiff rises in the prices of raw materials and capital goods. As in the past, the trade deficit was more than offset by receipts from services and capital inflows. A sizable overall payments surplus pushed foreign reserves up to $2.7 billion at yearend.

Flexible fiscal and monetary policies have been instrumental in assuring comparative price stability and high employment. Consumer prices increased only 13% in 1974. Unemployment decreased to 4%, compared with 4.5% a year earlier. Even in industries hit hardest by low export demand, layoffs were limited to 16,000 persons, many temporary workers brought in from neighboring Malaysia. The recently announced budget for FY 1975/76, while allowing for some job creation through public sector expenditures, calls for no appreciable tax increases.

Long-Term Factors

Since separation from Malaysia in 1965, the tiny island republic has capitalized on its strategic geographic position and outstanding managerial capabilities to become a major world trading and financial center. Singapore is the third largest oil refining center in the world and the focus of the Asian dollar market. It has emerged as the principal service zone for oil exploration and development in the region. Per capita income in 1974 exceeded $2,000. The economy is highly dependent on external trade and remains extremely sensitive to fluctuations in world markets.

For many years, the key to Singapore's development strategy has been its encouragement of foreign private investment in export-oriented, labor-intensive manufacturing industries. Through aggressive government solicitation, tax incentives, and low wage rates, Singapore has attracted substantial inputs of foreign capital, the largest share from the United States. By 1974 the book value of US investment totaled $600 million, mostly in petroleum refining, electronics, and light manufacturing.

Over the past year, the government has shifted its strategy toward capital-intensive, high-technology industries. This move was dictated by rising wage rates and tight labor markets, which reduced competitiveness in the established industries.

The government is pushing shipbuilding and repair, oil equipment construction, and iron and steel in preference to the slumping electronic, textile, and woodworking industries. Because of generally slack demand in advanced countries, investors are not rushing in to these new lines.

Outlook for 1975

The outlook for this year is for growth of 6% or more, the rate depending on global economic conditions in the second half. Commodity exports are expected to expand only moderately, but oil-related service industries should continue to grow in line with the rapid pace of exploration in the region. Banking and financial services should also remain strong, particularly if OPEC investment funds are channeled into the area. (Confidential)■

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Note

Copper Stocks Continue To Rise

Cuts in output by major copper producers – the equivalent of 500,000 tons of annual production – have failed to stem the rise in world inventories. Stocks now exceed 1 million tons, the highest in recent years. LME warehouse stocks reached a record high of 215,850 tons last week, dropping the world price to 56 cents a pound. CIPEC nations (Chile, Peru, Zambia, and Zaire) are resisting further cutbacks in output and can be expected to push harder for international financing of a buffer stock. (Confidential)

Publications of Interest*

USSR: Early Look at the 1975 Grain Crop
(ER IB 75-3, April 1975, Secret No Foreign Dissem)

This publication discusses the status of the Soviet grain crop, makes a preliminary estimate of production, and assesses the prospects for Soviet grain imports. Our early forecast puts 1975 Soviet production at 220 million tons, close to the 1973 record of 222.5 million tons.

OPEC Disbursements of Economic Assistance to Less Developed Countries, 1974
(ER IR 75-13, May 1975, Secret No Foreign Dissem)

This report brings together data on the expanding OPEC economic assistance program. It examines OPEC economic disbursements to the LDCs and to multilateral agencies in 1974 and evaluates the factors that will affect aid in 1975.

Prices of Machinery and Equipment in the People's Republic of China
(A (ER) 75-64, May 1975, Unclassified)

This handbook contains wholesale prices, in domestic currency (yuan), for a wide range of Chinese industrial products in 1952, 1957, 1965, and 1972. Where possible, full source references are given.

* Copies of these publications may be ordered by calling [redacted] Code 143, Extension 7234. 25X1A

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Correction

Some copies of last week's EIW had an incorrect series designator on the cover. It should have read ER EIW 75-17, 30 April 1975.

ECONOMIC INDICATORS

Prepared by

The Office of Economic Research

May 7, 1975

Foreword

The *Economic Indicators* provide up-to-date information on changes in the domestic and external economic activities of the major non-Communist developed countries. To the extent possible, the *Economic Indicators* are updated from press ticker and Embassy reporting, so that the results are made available to the reader weeks - or sometimes months - before receipt of official statistical publications.

Comments and queries regarding the *Economic Indicators* are welcomed. They may be directed to [redacted] of the Office of Economic Research, Code 143, Extension 7402 or 351-7402. 25X1A

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